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Supreme Court, U.S.
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No. 02-73

In the Supreme Court of the United States

STUDENT LOAN FUND OF IDAHO, INC.
Petitioner,

v.

UNITED STATES DEPARTMENT OF EDUCATION,
AND
RODERICK R. PAIGE, IN HIS OFFICIAL CAPACITY AS
SECRETARY OF THE UNITED STATES
DEPARTMENT OF EDUCATION,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

REPLY TO BRIEF IN OPPOSITION

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INTRODUCTION

Concerning the issues which Petitioner, Student Loan Fund of Idaho, Inc. ("SLFI"), asks the Supreme Court to review, the District Court stated, "The issues presented in this matter have been challenging, and considerable deliberation, review, research and analysis have been expended in reaching the final disposition." App. 88a. In this same vein, the Court of Appeals reflected that "we are asked to interpret a difficult contract and attempt to divine what the Congress meant in portions of the Higher Education Act (Act). The importance of the issues cannot be gainsaid, as they deal with loans to post-secondary students." App. 4a. As discerned by the lower courts, this case involves difficult and important issues which will have far reaching effects upon the ability of private parties and the government to enter into contracts for providing services and benefits to our nation's citizens.

Respondents' Brief in Opposition ("BO") emphasizes the importance of the issues, and also the necessity of granting certiorari, by arguing that the general rules of contract and statutory interpretation, which this Court has uniformly applied in all cases dealing with government contracts, should not be applied in the present case. The Court of Appeals' failure to apply rules which this Court has held should be applied warrants review by the Supreme Court.

ARGUMENT

I. General rules of contract construction apply.

Respondents argue that the rule requiring contract ambiguities to be read in favor of the non-drafting party does not apply to this case because ". . . a contract entered into by a government agency to carry out a regulatory program must, unlike commercial contracts between private parties, be interpreted in light of the regulatory program and the statutory

provisions that authorize it." BO at 17. Respondents attribute this distinction between commercial contracts and regulatory agreements to the Court of Appeals. However, the Court of Appeals makes no such distinction. The distinction made by the Court of Appeals is between contracts involving a federal agency and those involving private parties. The Court of Appeals states, "interpreting an ambiguous provision in a contract involving a federal agency is different from the same exercise when the contract involves private parties." App. 15a. The Court of Appeals then applies its own rule for resolving ambiguities "by consulting the Act, the regulations, and the policies behind them." App. 15a.

Although contractual provisions are to be read in light of the statutes, regulations, and policies, this should not be done to the exclusion of general rules of contract construction especially when the statutes, regulations and policies do not speak to the matters addressed in the contractual provisions. The contractual provisions at issue address termination of the contracts and, more specifically, voluntary termination by the guaranty agency. Nowhere in the Higher Education Act ("HEA") or the corresponding regulations is this issue addressed. However, the contracts clearly provide:

> "The Commissioner's obligations to make payments, as provided for in this Agreement, shall extend only with respect to loans insured by [SLFI] prior to termination of this agreement or prior to the expiration of the authority provided in the Act.
>
> This Agreement may be terminated by either party upon not less than 60 days written notice to the other party, except that the Commissioner may terminate this Agreement only for cause. Termination shall not affect

> obligations incurred under this Agreement by either party before the effective date of termination. If termination is effected by the Commissioner, it will not become final until [SLFI] has been afforded reasonable notice and an opportunity for a hearing, except that the Commissioner may suspend this Agreement pending the outcome of the hearing if he determines that such action is necessary in order to prevent substantial harm to the interests of the Federal Government." App. 123a.

At face value these provisions permit SLFI to terminate the agreements without affecting the parties' obligations, including the Secretary's obligation to make payments to SLFI with respect to loans insured by SLFI prior to termination.[1] Applying the general rule of contract

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[1] Respondents assert that the contract provisions and the statutory language authorizing the Secretary to enter into contacts with a guaranty agency and obligate the government to pay "the guaranty agency . . . for the life of the loans . . ." do not refer to an obligation to the guaranty agency but only to the loans and Respondents may therefore pay reinsurance to any guaranty agency of its choosing *without regard to which guaranty agency paid the claims*. To the contrary, Congress authorized the contracts for the purpose of encouraging state and private non-profit guaranty agencies to participate in the guaranteed student loan programs. No guaranty agency would have participated without a contractual right to receive reinsurance payments on the loans it guarantees. Further, Respondents' interpretation allows the Secretary to pay reinsurance to another guaranty agency *which did not pay the insurance claim to the lender*, thereby providing a windfall to the other guaranty agency. In the present case, the Secretary proposes paying reinsurance to the Northwest Education Loan Association

construction that ambiguities are to be construed against the drafter renders the same conclusion.[2]

In *United States v. Winstar Corporation et al.*, 518 U.S. 839, 116 S.Ct. 2432, 135 L.Ed.2d 964 (1996), the Court acknowledged that government contracts are subject to subsequent legislation "most if not all of the time." Based on

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for loans which are guaranteed *and the claims for which have been paid by SLFI*. Providing such a windfall was not the intention or purpose of the contracts or the statutes.

[2] The Court of Appeals suggests that SLFI's interpretation of this contractual provision would allow SLFI to receive the benefits of the contracts while operating outside the parameters of the Federal program and that SLFI would be able to lock in the ability to receive reinsurance simply by beating the Secretary to terminating the agreements. First, SLFI has never asserted that termination of the agreements would allow SLFI to operate outside of the Federal program. To the contrary, as found by the District Court and agreed by SLFI, although the agreements were terminated the obligations of both parties in existence at that time survive. Second, there has been no cause for which the Secretary could terminate the agreements. Respondents have had nearly eight years to show any basis or cause for terminating SLFI's agreements. 20 U.S.C. §1078(c)(9)(E) sets forth possible causes for termination. None of the causes listed in the statute have been shown to be present in this case although there have been ample opportunities to do so, including during the two-week trial, or during administrative proceedings for termination and suspension/debarment. Chief Administrative Law Judge Ernest Canellos ruled that although the agreements had been terminated the effect of such termination was an issue to be decided by the District Court. See App. 158a-162a. Chief Judge Canellos also held that Respondents had no legitimate cause for seeking suspension or debarment against SLFI's directors. See App.145a-157a.

this acknowledgment and using the Court of Appeals' analysis, the general rule whereby ambiguous terms are construed against the drafter would never be applicable to government contracts because the court could always infer an interpretation of the contract terms from the subsequent legislation, or, as in the present case, from the government agency's informal interpretations. The Court has made clear that this rule of construction applies to government contracts; however, it will never be applied in the Ninth Circuit due to the Ninth Circuit's rule for interpreting government contracts different from private contracts.

SLFI's Petition for Writ of Certiorari should be granted so that the Court can clarify if there are differing categories of government contracts for which different rules of interpretation apply. SLFI has found no case law, nor do Respondents cite to any, which supports the assertion that the government contracts at issue in this case should be treated different from other government contracts where the ambiguous terms of the contracts are construed against the government as the drafter of the contracts. The Court of Appeals' decision which applies different rules of construction for government contracts clearly contradicts rulings of this Court and therefore warrants review.

II. The Secretary's interpretation of "reserve funds" is not entitled to Chevron deference.

Prior to this litigation the only statement from Respondents identifying the federal interest in a guaranty agency's reserve funds is consistent with the position taken by SLFI in this case. In the August 1987 General Accounting Office report, the Assistant Secretary of Education over postsecondary education, including policy and regulation development, affirmed that the only Federal interest in guaranty agency reserves is in the Federal advances and once

an agency returned the advances then the regulations relating to reserve funds did not apply.[3] Assistant Secretary C. Ronald Kimberling affirmed this policy and interpretation in his deposition. App. 163a-176a; 178a-179a. Respondents now seek to disavow the statements of the Assistant Secretary claiming such statements "did not purport to interpret" the regulations. BO at 20.

The initial version of the regulations at issue were promulgated in the 1970's and applied solely to guaranty agencies receiving advances pursuant to 20 U.S.C. §1072(a). SLFI did not receive such advances therefore the regulation was not applicable. In 1985, Respondents consolidated the regulation pertaining to §1072(a) advances with the regulation pertaining to §1072(c) advances which had only required that §1072(c) advances and earnings on such advances be placed in a separate reserve account. As to this consolidation, Respondents formally stated that such regulations would:

> "establish requirements for the *maintenance and use* of an agency's reserve fund in §682.410(a). Except for restrictions on the use of loan insurance premiums, *current regulations governing the reserve fund apply only as long as the agency retains Federal advance funds. . . The proposed content and uses of the reserve fund are essentially the*

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[3] It is uncontested that SLFI has returned all Federal advances. App. 83a. Respondents' incorrectly state that in the District Court's view once advances were returned SLFI no longer had federal reserve funds. BO at 6. Although such a finding would be consistent with Respondents' longstanding position, the District Court held that because SLFI used *both* its regulatory reserve fund **and** returned the advances it no longer held federal reserve funds. App. 47a, 83a-86a.

> *same as the requirements in existing regulations. . .*" Fed. Reg. vol. 50, no. 171, Wednesday, Sept. 4, 1985, p. 35968. (Emphasis added).

Respondents' formal statement from the Federal Register are identical to the statements of policy and interpretation provided by Assistant Secretary Kimberling, namely, that the reserve fund regulations pertained to "maintenance and use" of reserve funds rather than ownership of such funds and that once an agency returned the Federal advances the regulations governing reserve funds no longer applied.[4] Prior to this litigation, Respondents never, formally or informally, promulgated any interpretation of the regulations which contradicts the statements of the Assistant Secretary or those made in the Federal Register.

Respondents cite to *Smiley v. Citibank (South Dakota) N.A.*, 517 U.S. 735, 742-743 (1996), for the assertion that Assistant Secretary Kimberling's statements "cannot be said to be inconsistent with the Secretary's regulation." BO at 20. The Court should recognize that the Assistant Secretary's

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[4] In his deposition Assistant Secretary Kimberling explained that the regulations no longer applied because once Federal advances were returned the government no longer had an ownership interest in the guaranty agency's reserve funds. Further, Assistant Secretary Kimberling testified that §682.410(a) was established for the regulation of reserve funds to insure the guaranty agency's ability to pay claims and not for the purpose of defining Federal ownership. App. 176a-178a. Respondents' position that the regulation defines the Federal interest in guaranty agency funds was not asserted prior to this litigation. *Several years after this litigation began*, Respondents promulgated a regulation asserting that §682.410(a) defines reserve funds for purposes of 20 U.S.C. §1072(g).

statements are not inconsistent with the regulation but only with a new interpretation of the regulation proposed by Respondents in the course of this litigation. Further, in *Smiley* the Court found that inconsistent statements of an agency official which were also contrary to agency statements in the agency's Notice of Proposed Rulemaking were not "sufficient in and of itself to establish binding agency policy . . ." *Id.* 517 U.S. at 743. The facts of this case are very different. Here the statements of the Assistant Secretary are consistent with Respondents' formal statements in the Federal Register and, at least prior to this litigation, there have been no indications, formal or informal, that the Secretary's position had changed.[5]

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[5] Respondents refer to the so called "spend down" cases to assert that the regulations defining reserve funds were "well-established." The "spend down" cases, however, interpreted and applied, not the regulations or statute at issue in the case, but rather, a statute which has since been repealed which included a statutory formula for determining "excess" cash reserves. See 20 U.S.C. §1072(e)(1988); App. 100a-101a.

Respondents assert that in the Student Loan Reform Act of 1993, Pub. L. No. 103-66, 107 Stat. 341-363, Congress codified the holdings of the "spend down" cases. SLFI maintains that the 1992 amendments to the HEA are part of this codification and references the Congressional reports accompanying the Student Loan Reform Act of 1993 for support. Petition p. 6. In either event, such 1993 amendment does not say what the Secretary and the Ninth Circuit assert, i.e., it does not say that the reserve funds "are the property of the United States" but instead that they are "considered to be the property of the United States . . ." Thus, raising the implicit question of considered for what purpose. Congress, answering this question, states, "to be used in the operation of the program. . . ." In the accompanying Conference Committee report to the 1993 Amendments the Congress refers to

Lending further support to Assistant Secretary Kimberling's statements, and SLFI's interpretation, is that when the federal interest in a guaranty agency's reserve funds are limited to Federal advances all of the provisions of the HEA are consistent and harmonized. However, rather than read all of the statutory provisions to be consistent the Court of Appeals defers to the Secretary's new position that would repeal by implication significant portions of §1072.[6]

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its understanding of the "spend down" cases by its reference to "judicially supported view that a guaranty agency's assets are dedicated to the loan programs and may not be used for any unauthorized purposes." App. 118a. The Secretary's position, which the District Court found to be beyond the scope of the statute (App. 83a), turns this statute on its head by asserting that any moneys used in the program, without regard to source, become part of the reserve and thereby Federal.

[6] Respondents' position that all funds and assets of SLFI are Federal property (See App. 142a-143a), besides being inconsistent with prior formal and informal statements, is inconsistent with the regulations and the Court of Appeals' decision. The Court of Appeals ruled that the regulations are entitled to deference. The regulations require that certain funds be credited to a reserve fund including "Other funds received by the guaranty agency from any source *for the agency's guaranty activities*." 34 C.F.R. 682.410(a)(ix). The District Court held, and it is uncontested, that "SLFI received substantial non-program related funds from private sources." App. 84a. Under the regulations such "non-program related funds" are not credited to the reserve fund; therefore, Respondents' interpretation which attempts to convert such into Federal property exceeds the regulation and is not entitled to deference. (The District Court found that all reserve funds (excluding the non-program related funds) had been properly expended in the payment of claims by September 1995 thereby necessitating SLFI's use of non-program

III. Survival of contract provisions does not interfere with the Secretary's authority to transfer loans.

Respondents repeatedly state that SLFI's interpretation of the contract providing for obligations which survive termination of the agreements, specifically, the Secretary's obligation to pay reinsurance, abrogates the Secretary's authority to transfer loans under 20 U.S.C. §1078(c)(8). However, Respondents and the Ninth Circuit completely ignore the wording of this statute which expressly requires that the Secretary may only direct the transfer of a loan "*for which the Secretary has made a payment pursuant to paragraph (1)* of this subsection. [i.e., a reinsurance payment]." 20 U.S.C. §1078(c)(8)(emphasis added). There is no conflict – if the Secretary pays reinsurance. Once paid he may then direct a transfer of the loan. Presently, the Secretary seeks, and the Ninth Circuit incorrectly authorized, the transfer of loans without paying reinsurance.[7]

CONCLUSION

The Ninth Circuit failed to apply the correct rule of contract interpretation and incorrectly afforded deference to Respondents' inconsistent and unsupported position which attempts to convert non-program related, private funds and assets into Federal property. For these reasons SLFI's Petition for Writ of Certiorari should be granted.

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related funds to fulfill its contractual obligations to lenders. App. 85a).

[7] Another statute, 20 U.S.C. §1078(b)(2)(E)(I), provides for the transfer of loans from one guarantor to another "with the approval of the holder of the loan." No such approval was sought or received by the Secretary. Absent lender approval, SLFI remains liable on its guarantees which explains why lenders continue to submit claims to SLFI (a fact Respondents ignore).

RESPECTFULLY SUBMITTED,

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APPENDIX O

UNITED STATES DEPARTMENT OF EDUCATION
WASHINGTON, D.C. 20202

Student Financial Assistance Suspension and Debarment Actions

Docket Nos. 95-05-DA-S [Consol.][1]

[Dated August 21, 1997]

In the Matter of	)
	)
Lewis M. Hall, John L. Magdiel, Carol Lee Lawhorn, Stephen E. Maloney, and Hal Turner,	)
	)
Respondents.	)

Appearances: Robert C. Montgomery., Esq., Fruitland, Idaho, for the Respondents.

[1] The following cases have been consolidated herein: Docket Nos. 95-6-DA, 95-7-DA-S, 95-8-DA, 95-9-DA-S, 95-10-DA, 95-11-DA-S, 95-12-DA, and 95-13-DA-S, and 95-14-DA.

Student Financial Assistance
Suspension and Debarment Actions

Brian P. Siegel, Esq., Office of the General Counsel, United States Department of Education. Washington, D.C., for Student Financial Assistance Programs.

Before: Chief Judge Ernest C. Canellos

DECISION

The Respondents are the five Directors of the Student Loan Fund of Idaho (SLFI), a private, nonprofit corporation organized under the laws of Idaho. SLFI had been the designated guaranty agency for the State of Idaho in the Guaranteed Student Loan (GSL) Program, in accordance with §428(b) of the Higher Education Act of 1965, as amended (HEA); such a designation was implemented by five agreements between SLFI and the U. S. Commissioner of Education dated July 20. 1978.[2] The office of Student Financial Assistance Programs (SFAP), U. S. Department of Education (ED), oversees the federal student financial assistance programs authorized by the HEA including the GSL and FFEL programs.

- Procedural History -

On November 20, 1994, each board member was

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[2] The authority of the U.S. Commissioner of Education currently resides in the Secretary of Education, The GSL program is currently called the Federal Family Education Loan (FFEL) program.

issued a separate Notice of Proposed Governmentwide Debarment and Suspension from Federal Nonprocurement Transactions pursuant to 34 C.F.R. § 85.312 and 34 C.F.R. § 85.411. In the notices, which are identical except for separately naming the Respondents, SFAP alleges that the Respondents "willfully failed to perform in accordance with public agreements between the Department and SLFI and have failed to comply with directives issued by the Department" and, as such, they are subject to debarment under 34 C.F.R. § 85.305(b).[3] In response to the notices, on December 29, 1994, the Directors of SLFI requested hearings in both the debarment and suspension actions. The Respondents, *inter alia,* moved to join the debarment and suspension actions of all of the Directors and I consolidated these actions on March 31,1995.

On April 18, 1995, the Respondents moved that I suspend the proceedings until the issuance of a decision on an action which SLFI had filed in the United States District

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[3] 34 C.F.R. § 85.305 **Causes for Debarment** provides, in part:

Debarment may be imposed... for:

...

(b) Violation of the terms of a public agreement or transaction so serious as to affect the integrity, of an agency program, such as:

(1) A willful failure to perform in accordance with the terms of one or more public agreements or transactions;

Court for the District of Idaho.[4] Although SFAP originally objected to the stay, it subsequently withdrew such opposition, and on May 2, 1995, I granted the motion. On September 14, 1995, the District Court issued orders on the substantive motions. The Respondents requested that the stay be continued; SFAP opposed; and after a conference call with the parties, I granted the stay pending an appeal of the District Court's Orders to the United States Circuit Court of Appeals for the Ninth Circuit. On December 13, 1996, the Ninth Circuit issued a Memorandum decision in which it reversed the District Court's decision relative to summary judgement and remanded the case back to the District Court for a trial on the merits. SFAP requested that the Ninth Circuit reconsider its decision which the Court denied. Subsequently, after I determined that no further postponements were appropriate, on June 25, 1997, I held an oral argument. Subsequently, the parties filed post-hearing briefs and I took the case under advisement.

-Facts and Issues -

Although the procedural history of this case has been long and circuitous, the underlying substantive issues are relatively simple and straightforward. As a background, the facts reveal that SLFI became convinced sometime prior to 1992, that because of changes Congress made to the HEA, its participation in the federal student financial assistance

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[4] On March 28, 1995, SLFI filed a Motion for a Writ of Mandamus. Contemporaneously, the District Court was considering ED's Motion for Summary Judgement and Judgment on the Pleadings on the same issues.

programs as a guaranty agency was no longer financially feasible. SLFI determined to end its status as a guarantor and, to that end, negotiated with the Northwest Education Loan Authority (NELA), the guaranty agency in the neighboring state of Washington, to transfer such responsibility to it. Part of those negotiations revolved around SLFI continuing to carry out business as a servicing agent for NELA's Idaho transactions, The two agencies reached an agreement in principal and on April 22, 1994, SLFI informed ED that it was providing the 60 days written notice of termination required under the agreements between SLFI and ED; and that, pursuant to that notice, those agreements would be terminated at the close of business on June 30, 1994. The Respondents claim that SLFI's letter was clear and showed its purpose was to cease guaranteeing any new loans but continue to service all of its existing guaranty obligations.[5]

ED's reaction was swift and direct. SLFI was informed that it had no authority to engage in discussions with NELA, any agreement between those parties was a nullity, and that ED would decide who would be designated as the new guaranty agency for Idaho. Interestingly, after considering the issue, SFAP decided that, indeed, NELA was the appropriate agency to be designated the new guarantor, however, it refused to approve the continued participation of SLFI as a servicer absent a clear showing that the arrangement was cost effective for the FFEL Program. To

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[5] The April 22, 1994 letter provides, "Please accept this letter as the 60 day written notice of termination required in out agreements. We will guaranty no additional loans under your program after June 30, 1994."

effectuate the transfer of guaranty agency responsibility from SLFI to NELA, on May 31, 1994, SFAP directed that SLFI, "transfer its outstanding guarantees, the defaulted loan portfolio, and all of its reserve funds and assets to NELA." Later, on September 20, 1994, SLFI was directed to cease and desist any activities involving the FFEL Program. SLFI refused to comply with these directives on two basic grounds. First, some of its assets were its separate property and should not be turned over. Second, since the rules require that lenders must approve a transfer of guarantees from one agency to another, SLFI could still have contractual liability for its guarantees even if they were transferred to NELA. Ultimately, relations between SLFI and SFAP became strained and then acrimonious, the result of which was that the lawsuits were filed and the subject actions were initiated.[6]

It is readily apparent that there are two separate courses of action which are being pursued contemporaneously and one of the threshold questions is how do they interact. The first one involves the substantive issue of whether SLFI is in violation of its agreements with ED and if so, what is SLFI's resulting liability. Included therein is the question of how much of SLFI's funds and property should be characterized as federal assets and, therefore, returnable to ED or its designee. Without question, that issue is before the District Court and I have no jurisdiction to influence that

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[6] In addition, on February 20, 1996, SFAP initiated an action to terminate the agreements between SLFI and ED under which SLFI acted as a guaranty agency, and impose an emergency action. I was the hearing official and, on May 21, 1996. I dismissed both actions as moot.

resolution. The other issue involves the five Respondents in this suspension and debarment case, over which I have the exclusive authority to decide. After the Ninth Circuit had issued its decision which found, in part, that a statutory predicate to the demand for return of funds had not been met by the Secretary, I posited the following to the parties, "[T]herefore the ultimate issue, here, is whether the Respondents may be held accountable, by the imposition of a debarment action, for the failure of SLFI to return funds over which a genuine dispute exists as to what amount of the funds are owed to the Federal government." In response to my solicitation of the parties' views on my observation, SFAP argued that "the Ninth Circuit's action is irrelevant to this proceeding since it does not address the individual Respondents' failure to comply with the directives from the time they became effective until the date the Ninth Circuit issued its decision." Also, SFAP argued that "the directives issued by the Department directed SLFI and its directors to turn over defaulted loans and outstanding guarantees to the successor agency designated by the Department; cease and desist from the use of reserve funds without prior approval of the Department; and turn over reserve funds and reserve fund assets to the Department," something they have failed to do.[7]

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[7] Although SFAP insists that such a "best interest" determination had been previously made, on March 7, 1997, the Assistant Secretary for Postsecondary Education issued a letter addressed to the Chief Executive of SLFI, which states, "This letter constitutes our determination that the return of federal funds by the Student Loan Fund of Idaho (SLFI) is in the best interest of the Federal Family Education Loan (FFEL) Program. This determination is being made pursuant to the authority given to the

As previously mentioned, the Respondents view the Ninth Circuit's action as removing all possible bases for the debarment and suspension actions.

- Discussion -

As an initial observation, and despite SFAP's protestation to the contrary, I find that the merits of the dispute between SLFI and ED relative to SFAP's directives enumerated above are inextricably interwoven with the suspension and debarment actions before me. Any other decision would defy credulity. To hold individuals personally accountable for failing to comply with directives without determining what those directives were, or whether they were a legitimate exercise of authority, would certainly not comport with due process.

SFAP's contention that SLFI was obligated to comply with the ED's directives irrespective of the appropriateness of the directive appears to be at odds with the purpose for which debarment proceedings are used. The fulcrum of SFAP's argument rests on the assumption that upon receipt of the Department's directive, the SLFI board members had no choice other than to vote to comply with the Directive. As a factual matter, SFAP's assumption was not only unfounded, but incorrect since the Ninth Circuit determined that the directives were procedurally defective and without legal effect. According to the Ninth Circuit, "[t]here was no evidence that the Secretary had made a 'best interest'

Secretary of Education by statute. 20 U.S.C. § 1072(g)(1)."

determination" as required by 20 U.S.C. 1072(g)(1). The Ninth Circuit found that the May 16, 1994 and September 20, 1994 letters to SLFI from the Department "do not satisfy, the statutory condition that the Secretary determines that such return is in the best interest of the operation of the program." Given that the Ninth Circuit determined that the Secretary had not met the statutory condition providing him with the requisite authority to require SLFI to return reserve funds to SFAP, it would be anomalous to find that the SLFI board members were, nonetheless, subject to debarment simply because SLFI challenged the correctness of the Department's directive without first following it. In this respect, I find SFAP's argument, that the fact that the SLFI board members' failed to vote to comply with the Department's directives warrants each board members' debarment, unpersuasive.

As a general premise, in any debarment action the burden of proof is on ED. 34 C.F.R. § 85.314(c)(2). The causes of debarment must be established by a preponderance of the evidence. 34 C.F.R. § 85.314 (c)(2). Generally, the existence of a cause for debarment does not necessarily require that the individual be debarred, rather the seriousness of the omissions and any mitigating factors must be considered in making the debarment decision. 34 C.F.R. § 85.300. Here, even assuming that SLFI violated SFAP's directives so as to make it subject to debarment, SFAP presented no direct evidence of which, if any of the Respondents made or were otherwise, responsible for the decisions enumerated above. Of course, it is sometimes impractical for ED to uncover who is responsible for business decisions -- such decision-making processes are often not revealed. In recognition thereof, and in order to help to

correctly attribute fault, the regulations provide that the "fraudulent, criminal or other seriously improper conduct of a participant may be imputed to any .... director .... who participated in, "knew of, or had reason to know of the participant's conduct." 34 C.F.R. § 85.325 (b)(2). This imputation allows for the debarment of individuals for decisions they made for their principals. However, the imputation is limited to "fraudulent, criminal, or other seriously improper conduct," and not any lesser conduct. *See generally, In re Marcus Katz*, Docket No, 93-115-DA, U.S. Dep't of Educ. (January 18, 1994)

With that background, I will review the facts of the cases before me. The evidence or record reveals that SLFI determined to change its status as a guaranty agency which it had under agreements with ED; such change would include, at a minimum, that there would be no new guarantees after June 30, 1994. To effectuate that change, SLFI entered into an agreement with NELA that NELA would guaranty all new loans in Idaho and SLFI would turn over all the old guarantees and the "corresponding reserve funds." SLFI claims that it wished to continue in the program but in a modified manner, i.e. that it would continue to service existing guarantees because it was contractually obliged to do so and it would service NELA guarantees in Idaho. When SFAP was apprised of that situation, it refused to agree. SFAP basically decided that a designated guaranty agency had to either fulfill all program requirements of that function or remove itself completely. Therefore, NELA would be designated as the guaranty agency for Idaho, but NELA could not contract with SLFI unless NELA could show convincingly that such a set-up was cost effective. SFAP's position

effectively undermined the NELA-SLFI agreement and it was abrogated. In a May 31, 1994 letter, SFAP directed SLFI "to transfer its outstanding guarantees, the defaulted loan portfolio, and all of its reserve funds and assets to NELA." This demand was modified by a September 30, 1994 letter to provide, "This transfer must include the transfer of all legal ownership and control of SLFI's assets to NELA, including: defaulted loans; outstanding guarantees; any and all funds, in whatever form; SLFI's 'Reserve Fund'; SLFI's 'Operating Fund'; and all physical assets wholly or partially owned by SLFI."

It is interesting to note that at an initial hearing that I held by conference call, counsel for SFAP agreed that some of SLFI's funds were probably not federal funds and that SFAP was ready to negotiate over that issue. This negotiation, however, was to be accomplished only after SLFI had turned over all its funds to NELA -- if the negotiations culminated in an agreement that some of the funds were, in fact, really SLFI's, they would be returned. Since then. SFAP's position has changed somewhat -- all the funds must be returned because, although it has been given every opportunity to do so, SLFI has not presented any evidence to show that the funds are independently their own. SLFI disputes that it has not provided sufficient information establishing its entitlement to certain funds, and argues that following SFAP's directives would effectively put it out of business, something they could not recover from even if they subsequently prove that they were correct all along. Without submitting any evidence to that effect, SLFI alludes to bad faith on the part of SFAP, attributing SFAP's position to its desire to assist the administration's Direct Lending Program by discouraging its

natural competitor, the FFEL program and its participants.

The main thrust of SFAP's theory of the case is that the Respondents are fiduciaries, and their failure to comply with SFAP's directions breached their fiduciary duty -- debarment is appropriate for this dereliction. On the other hand, the Respondents point out that, regardless of the type of duty they owe ED, under state law, they are held to the standard of a fiduciary and have a duty to safeguard the corpus of their nonprofit corporation. Put in perspective, SFAP asserts that the Respondents owe it a duty to immediately comply with its directives, including those dealing with the turning over of all of SLFI's assets to a third party, with whom SLFI has no enforceable agreement, with an unsecured promise that if SLFI were able to establish that some of the assets were their own, they would be returned (by NELA). Contrariwise, the Respondents argue inferentially that complying with SFAP's directions would violate their fiduciary duties as enumerated above. According to the Respondents, their only solution to this conundrum of conflicting duties, was to refer this and all other associated issues to a court of proper jurisdiction and await its decision. This they point out they have done, therefore, they should not be subject to debarment. The Respondents argue further that SFAP's property interests are secure and protected since its records were reviewed by ED's Inspector General (IG) and the record indicates the IG found no failings therein, and the District Court was sufficiently satisfied of that fact so as to deny ED's request for the posting of a bond pending the Court's decision. As was mentioned earlier, all questions regarding who owns SLFI's property is solely within the jurisdiction of the District Court. The only relevance of those

questions to these debarment and suspension actions is to recognize that there is clearly a dispute on that issue, and how the fact that there is such a dispute may have an impact upon my decision as to the Respondents' culpability in debarment.

The debarment of an individual has serious consequences -- that individual is precluded from participating in any way in a covered transaction under the nonprocurement programs of any Federal agency, and is not eligible to receive any financial or nonfinancial assistance or benefits from any Federal agency. 34 C.F.R. § 85.100. However, it is the policy of the Federal Government to conduct business only with responsible persons, and debarment and suspension actions are appropriate means of implementing this policy. 34 C.F.R. § 85.115. In conjunction therewith, debarment and suspension actions may only be utilized to protect the public interest and may not be used for purposes of punishment, 34 C.F.R. § 85.115 (b). As to the basic issue of these proceedings, i.e. whether the Respondents' actions were sufficiently egregious under the circumstances so as to support debarment: my review of the evidence reveals that the answer is clearly "no." Therefore, I find that SFAP has failed to meet its burden of establishing that the five Respondents should be debarred.

On the basis of the foregoing, it is hereby ORDERED that the debarment and suspension actions are DISMISSED.

/s/_____
Ernest C. Canellos
Deciding Debarment and Suspension Official

Dated: August 21, 1997

APPENDIX P

UNITED STATES DEPARTMENT OF EDUCATION
WASHINGTON, D.C. 20202

Student Financial Assistance
and Show Cause Proceedings

Docket Nos. 96-19-ST and 96-22-EA

[Dated May 21, 1996]

In the Matter of	)
	)
STUDENT LOAN FUND OF IDAHO	)
	)
Respondent.	)
	)

Appearances: Robert C. Montgomery., Esq., Fruitland, Idaho, and John J. Keohane, Esq., New York, New York, for the Student Loan Fund of Idaho.

Brian P. Siegel, Esq., Office of the General Counsel, United States Department of Education. Washington, D.C., for Student Financial Assistance Programs.

Before: Judge Ernest C. Canellos

Student Financial Assistance
And Show Cause Proceedings

DECISION

The Student Loan Fund of Idaho (SLFI) is a private, nonprofit corporation organized under the laws of the State of Idaho. On June 13, 1978, SLFI was appointed by the Governor of Idaho to act as the designated guaranty agency for the State of Idaho in the Guaranteed Student Loan (GSL) Program, in accordance with §428(b) of the Higher Education Act of 1965, as amended (HEA).[1] To effectuate this designation as the guaranty agency, SLFI and the United States Commissioner of Education entered into a series of five agreements on July 20, 1978, which agreements governed how SLFI would carry out its functions as a guaranty agency.

By notice dated February 20, 1996, the office of Student Financial Assistance Programs (SFAP) notified SLFI that it was intending to terminate the agreements under which SLFI participated as a guaranty agency. SFAP cites §428(c)(9)(E)(4) of the HEA and 34 C.F.R. §682.413(c)(1)(iv) as authority for such action. This same notice imposed an Emergency Action against SLFI in accordance with the provisions of 34 C.F.R. § 682.413(e)(2)(i) and 682.704(a). In response to the notice, on March 8, 1996, the Executive Director of SLFI requested a hearing in the termination action and an opportunity to show cause why the emergency action was unwarranted.

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[1] The GSL program is currently called the Federal Family Education Loan (FFEL) program.

Pursuant to a delegation of authority from the Secretary to conduct proceedings and issue final decisions in both of these proceedings, I was assigned this matter on March 26, 1996. I issued an Order Governing Proceedings on April 2, 1996, in which I required the parties to address, as a threshold issue, the extent of my jurisdiction in this matter.[2] The parties submitted briefs, procedural issues were resolved, and a teleconference was held on May 15, 1996. During my dialogue with counsel for both parties during the teleconference, it became clear that the parties concurred that SLFI had voluntarily terminated its guaranty agency agreements effective June 10, 1994. As a result of such apparent concurrence, the parties were directed to attempt to enter into a stipulation which reflected this understanding. The parties were unable to arrive at a stipulation because of their stated disagreement as to the consequences of the termination of the agreements, but readily proffered that the agreements were terminated. Each of the parties submitted a timely draft order for my signature. Both draft orders contain the following identical language:

> I. The Office of Student Financial Assistance Programs (SFAP) and the Respondent, Student Loan Fund of Idaho (SLFI) stipulate that: (a) on April 22, 1994, SLFI informed the Department of Education (ED) that it was providing the 60 days written

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[2] In its notice, ED states that it believes that SLFI previously had terminated its guaranty agency agreements and that the termination action was initiated to resolve any possible question regarding SLFI's status in the FFEL program.

> notice of termination required under the agreements between SLFI and ED; and (b) that, pursuant to that notice, those agreements [were] terminated at the close of business on June 30, 1994.

In a show cause proceeding, the guaranty agency has the burden of persuading me that the emergency action is unwarranted. 34 C.F.R. § 682.704(d)(2)(ii). Further, pursuant to the provisions of 34 C.F.R. § 682.704(a), an emergency action should be upheld if: (1) there is reliable information that the institution is violating a provision of Title IV; (2) immediate action is necessary to prevent the misuse of federal funds, and (3) the likelihood of loss from the misuse outweighs the importance of adherence to the procedures for termination actions. However, in a termination action, it is ED which has the burden of proving that the agreements should be terminated. In either case, it is obvious that there must be a viable pre-existing agreement between the parties for me to have jurisdiction to determine whether the parties met their respective burdens; otherwise, I have nothing to decide. Consistent with the stated position of the parties, I find that the guaranty agency agreements between SLFI and ED were effectively terminated by SLFI in 1994, and, as a result, my jurisdiction to consider whether the termination or emergency action is warranted is necessarily eliminated. Since I have determined that I lack jurisdiction over this matter, I can not reach any of the substantive questions raised bv the parties.

ORDER

On the basis of the foregoing, it is hereby ORDERED that the termination and emergency actions imposed against the Student Loan Fund of Idaho are DISMISSED.

/s/_____
Judge Ernest C. Canellos

Dated: May 21, 1996

APPENDIX Q

Deposition Excerpts of C. Ronald Kimberling
February 5, 1997

[p.34]

Q. I want to ask you the same thing about Exhibit 2, which as I already indicated is entitled Guidelines for Reducing Guaranty Agency Reserves.

A. Okay. And I'm looking at this exhibit because I probably may find another clue as to why the GAO pursued this line of inquiry. All right. There is a letter at the front of the report dated August 7, 1986, addressed to the Honorable William D. Ford, who is the Chairman of the Subcommittee on Postsecondary Education in the US House of Representatives.

And in the first paragraph it refers to this as a briefing report and indicates that it responds to an April 29th, 1986, request by the subcommittee that the GAO provide guidelines for determining the maximum amount of cash reserves needed by guarantee agencies. So based upon that writing, it's my understanding that this particular report was in response to a direct [p.35] request by the congressional subcommittee that was in charge of authorizing the GSL program.

Q. Exhibit 2 is, not counting the title page, 49 pages long, and a portion of it labeled Appendix III includes a memorandum dated June 19, 1986, the third page of which contains your, or what I believe to be your signature, and then

a short memorandum, and that's pages 38 through 41 of Exhibit 2. Would you refer to those pages, please?

A. Uh-huh, yes.

Q. Would you take a second to review that and tell me whether that is indeed your signature on page 40 of Exhibit 2?

A. That is indeed a true copy of my signature.

Q. And tell me the purpose of pages 38 through 40 and why they appear with this report.

A. As I had explained a few minutes ago, it normally was the practice of the GAO before issuing any final report to Congress to prepare a draft report and to share that report with the cognizant agency that administers or administered the program they were studying and to solicit any comments that the agency wished to make with [p.36] respect to the draft report.

And generally then the agency's comments, or at least a summary of the agency's comments, would be included as an appendix to the final report so that Congress would have the benefit of both the GAO's views and observations and the agency's views and observations.

Q. And the reports were from you in your capacity as assistant secretary for postsecondary education. Is that correct?

A. That is correct. This appendix is styled as a

memorandum, and it's addressed from me in my capacity as assistant secretary for postsecondary education to the gentleman who was associate director of the human resources division of the GAO.

Q. At the time you authored this memorandum in June of 1986, was there any higher ranking person in the Department of Education overseeing postsecondary education?

A. I need to understand the question in terms of what you mean by overseeing.

Q. Well, describe for me in June 1986 to the extent postsecondary education was monitored or run or overseen by the Department of [p.37] Education. Describe for me the chain of command that would have been in place as responsible for those activities.

A. Okay. Well, the reason I asked clarification of the question was your use of the term "oversee." I was the highest ranking official responsible for the management and the administration, the policy development to some extent,, the policy articulation or decision making, and certainly the policy explication of those programs. There were other components of the US Department of Education that would have been involved in broadly overseeing the programs.

For example, the office of inspector general had authority to conduct compliance audits and criminal investigations, you know, with respect to those programs. In terms of organizational rank, I was equal in rank to the inspector general of the Department. I might also, you know, believe that the under-secretary of education who ranked

above me and the secretary of education who ranked above me, you know, certainly outranked me to the extent that they may have wanted to reserve unto themselves [p.38] the authority to make certain decisions. As a matter of general practice, they delegated officially and unofficially to me all of those responsibilities.

Q. Those included management, administration, articulation and explication?

A. And development and decision making of policies within the executive branch of government.

Q. And at that point in time William Bennett was the secretary of education?

A. That is correct.

Q. And then there's a memo, a one-page memo, the same type form as this appendix. Do you see that?

A. Yes.

Q. Did you provide that?

A. Yes. That actually is - - what' s on page 41 of the report is still part of Appendix III, and it is approximately one half a page of writing, and it is internally referred to on page 39, the second paragraph of that.

Q. Would other members or employees of the Department of Education have been involved in the discussions which led to pages 38 through 41 [p.39] being

included as part of the GAO report?

A. Yes.

Q. And describe for me who the other Department of Education employees would have been.

MR. SUBAR- Objection. This is just a -- I'm going to object to the form. I'll tell you why. You're asking who they would have been or who they were.

Q. (By Mr. Jones) Well, who they were. And not necessarily by identity. If you can give us that, great, if not, who would generally have been involved in those kind of -

A. All right. Well, let me start with individuals that I have a direct recollection of having been involved in the preparation of this document or the review of this document to one extent or another. It's my recollection that Mr. Larry Oxendine, O-X-E-N-D-I-N-E, was involved. I cannot -- at that time Mr. Oxendine either was the chief of the GSL policy branch within what we called the policy development division I believe was our term. It was a division, and it had branches covering each of the major Title IV programs, or he was the deputy director of the [p.40] division.

My recollection is that during my tenure initially Mr. Oxendine was the branch chief and that at some point in time during my tenure as assistant secretary he became the deputy director of the division with some continued specialization and involvement in the GSL program. And I don't remember in which capacity he functioned as of June 1986, but I directly recall his involvement simply because I recall a meeting with

Mr. Gainer, to whom this memorandum is addressed, and another gentleman from the GAO, Mr. Chris Chrissman, who was involved with this report, as I recall, and that Mr. Oxendine was present and fairly involved in the discussion.

The other person I recall having been involved was Mr. William Moran, who was the director of the policy development division and was Mr. Oxendine's – either his immediate superior or his superior once removed. The third person that I recall having had involvement more in a review capacity than a development capacity was Mr. Noel Kard, K-A-R-D, who was a Schedule C appointee and served as my chief of staff, and typically directly reviewed important -- not [p.41] every document, but important, documents that came up for my signature and approval. There may have been others involved in this preparation, but I'm not -- and most likely they would have been in the office -- or the policy development division, but I'm not aware of who they specifically would be.

Q. Pages 38 through 41 of Exhibit 1 were an expression of your view or the Department of Education' s view or both?

MR. SUBAR: Object as to form.

A. They were an expression of the Department of Education's view. Well, I've briefly read through this. Probably components of it were views that I strongly personally held, but I did not see it as my role to inject personal views into expressions of departmental policy in a formal report such as this.

Q. (By Mr. Jones) So what was pages 38 through 41 of Exhibit 1? You just used a phrase -- read back his last answer for me, please.

(Whereupon, the requested portion of the record was read by the reporter.)

Q. (By Mr. Jones) Were pages 38 through 41 [p.42] of Exhibit 2 an expression of official department policy?

MR. SUBAR: Object as to form and asked and answered.

A. I'm sorry, I didn't hear the last part.

MR. SUBAR: She heard it.

A. Yes, they were an expression of official departmental policy, or in some cases I guess some aspects of this are opinion or recommendation, but broadly they fall under policy to me.

Q. (By Mr. Jones) I'm going to ask you about a couple of specific things. The first thing I want to ask you about is on page 41, the last sentence of the first full paragraph, and tell me whether I read this correctly. "Once the federal monies are returned to the federal government, the use of the reserve fund is no longer restricted by federal regulations." Did I read that correctly?

A. Yes.

Q. And tell me what you meant by that?

A. Well, first the words "federal monies" here need to be taken into the context of the topic in the report. The report - - or this [p.43] appendix is specifically talking about reserve funds established by guarantee agencies. And it is my understanding that the term "federal monies" in this sentence refers to Federal Government advanced funds, and I believe that term or a term similar to it is used earlier in this paragraph, so it's not just any old federal monies. It's monies that the Federal Government had provided at one time or another to guarantee agencies to help them establish or augment their reserve funds. You wanted my fuller understanding of the sentence? Okay. I think that's the most important clarification that I can make.

It is -- the way I understand that sentence, it is an expression of the US Department of Education's interpretation or view of the then extent policy that whatever federal regulations were in place that the government uses, permitted uses of guaranteed reserve funds, would not apply to a guarantee agency on an agency by agency basis. It would have to be once the federal reserve advances were returned to the Federal Government. I'm closely paraphrasing it, but that's my understanding of what that sentence [p.44] means.

Q. Sure. And by the point in time when this was authored in June 1986, had you worked with or become familiar with the way the Guaranteed Student Loan program worked and the way the guarantee agencies interacted with the Department of Education?

A. I was fairly familiar with the way the program -- well, more than fairly familiar. I had a very good knowledge of the mechanics of how the program operated and

the role that guarantee agencies played as a component of how the program operated. That is and was such a complex program, I'm not sure that a single individual on the planet knows every single thing about the program.

Q. I think Judge Boyle would appreciate that. This statement that I've read into the record and asked you some questions about, was that statement consistent with your understanding of the industry-held view?

MR. SUBAR: Object as 5o form.

A. I -- what do you mean by industry-held view?

Q. (By Mr. Jones) The view of guarantee [p.45] agencies based on the work they'd done with the Department of Education leading up to June 1986.

MR. SUBAR: Object as to form.

A. I don't know. I don't – well, let me -- I met from time to time with representatives from the organization that collectively represented the various guarantee agencies. It goes by initials NCHELP, -C-H-E-L-P, National Council of Higher Education and Loan Programs, and their offices and their executive director were housed in Washington. When I say from time to time, on one basis or another I probably had some involvement on at least a monthly basis because that organization sent its representative to a monthly meeting that I, as assistant secretary, held with a number of higher education organizations.

I also from time to time had occasion to meet with the

executive directors of some different guarantee agencies. So from those interactions, I had some picture in mind of what the guarantee agency views were on a number of issues involving the program. But having said that, I don't have any recollection as to whether there was an industry-held view on the specific [p.46] topic of what would happen to reserve funds after the Federal Government component was remitted back to the Federal Government that was ever communicated to me. It's a pretty long sentence, but I hope you know what I meant.

Q. Did the sentence that I asked you about on page 41 of Exhibit 2 generate any controversy at the time?

A. I don't recall any controversy over this particular sentence.

Q. You didn't have outcries from NCHELP or state guarantee agency directors on the one hand or Department of Education employees on the other disputing the accuracy of the sentence we've been talking about on page 41 of Exhibit 2?

A. Nothing that ever -- it never reached my awareness. If there ever were such disputes, and I don't know that there were such disputes, I had absolutely no awareness of them.

Q. Was it or was it not accepted at least as of June 1986 that as to reserve funds held by state guarantee agencies, either *nonprofit* or state operated agencies, that as to those reserve funds, there would be both a federal component and a nonfederal component?

MR. SUBAR- Object as to form.

A. Can you restate that question again?

Q. (By Mr. Jones) Sure. Was there any question prior to June 1986 when pages 38 through 41 were generated that as to state guarantee agencies, either those nonprofit private corporations or state operated corporations that as to the reserve funds held by those agencies generally there would be both a federal component and a nonfederal component?

MR. SUBAR: Object as to form.

A. Generally not. However, it' s my recollection that at that time there were already a few guarantee agencies that had completely paid back the federal advance funds, and I don' t recall which ones specifically did so. I do recall that there were some that had. Therefore, with respect to those agencies that had paid back all of their federal funds, there would not have been a view that those agencies had both a federal and a nonfederal component since at that point in time with respect to those agencies it was entirely a nonfederal component. So with that exception or caveat, my recollection is that at that time most of the guarantee agencies had [p.48] some kind of mixture of federal and nonfederal funds making up their reserve funds.

Q. And as to the exceptions to that rule, there were agencies which had only nonfederal funds?

A. As far as I know, yes. Theoretically, it might have been possible for an agency to have only had federal funds and never have put in any other funds into its research

fund, but I was not specifically aware whether there were any such agencies.

* * *

[p.63]

A. Yes, yes. Without my specific approval of any proposed rule, it would not have gone on for final approval by the Secretary of Education.

Q. And did this language reflect the policy of the Department of Education?

A. Yes, just axiomatically, all regulations, all final regulations represent the absolute policy of the Department. All proposed regulations, though they have not become final, reflect the Department's policy as articulated in them.

Q. I want to ask you about two specific sentences, and I'll read the sentence first and then I'll ask you whether I read it correctly and then I'll ask you a question about it.

A. Uh- huh.

Q. The sentence reads, "Except for restrictions on the use of loan insurance premiums, current regulations governing the reserve fund apply only as long as the federal agency -- or as the agency retains federal advanced funds." Did I sort of read that correctly?

A. You read that correctly.

Q. That was the then policy of the [p.64] Department of Education. Is that correct?

MR. SUBAR: Object as to form.

A. I think it - - it's a statement of what the Department's policy then was.

Q. (By Mr. Jones) And of course that's referring to current regulations, and what is proposed in the entirety of the document from which Exhibit 3 is taken is proposed additions to those regulations. Correct?

A. That's correct, additions, deletions or amendments too.

Q. So I want to ask you about one other sentence, and I'll try and read this one correctly. "The proposed content and uses of the reserved fund are essentially the same as the requirements in existing regulations." Did I read that correctly?

A. Yes.

Q. So that the changes contemplating the proposed rules to the effect they were substantive did not affect the content or use of the reserve fund?

MR. SUBAR: 0bject as to form.

A. Correct .

Q. (By Mr. Jones) Because they' re

* * *

[p.83]

Q. Did the Department of Education during your tenure from 1981 to 1988 ever have the view that everything that showed up on a balance sheet of a guarantee agency was federal property?

MR. SUBAR: Object as to form.

A. No, not to my knowledge. I don't recall that view being expressed.

Q. (By Mr. Jones) In a previous response you made a distinction between ownership of the funds by the Federal Government on the one hand and regulation of guarantee agency activities on the other. Would you expand for me on the difference in your view?

MR. SUBAR: Object as to form.

A. Okay. The Federal Government can regulate the conduct, legally regulate the conduct of individuals and entities in a variety of different ways, and it can regulate the conduct of individuals and entities in terms of conduct that is not subsidized, funded, supported [p.84] in any way by the Federal Government.

An example of this would be some of the equal employment opportunity laws where discriminatory conduct is regulated by the Federal Government in areas where the Federal Government is not involved in any aspect in financing

or subventing the costs of such conduct. And then it also regulates the conduct of individuals and entities that are involved as participants or delivery elements of federal programs.

And it's in the latter sense that I would look at, you know, the role of the guarantee agencies as regulated entities because they do receive and did receive at the time we're talking about subsidies from the Department of Education. But given that those subsidies were authorized by Congress and that funds were appropriated for the programs, specific program purposes pursuant to that authorization, then in those cases where funds were lawfully appropriated and distributed by the Department of Education and lawfully received by qualified entities such as guarantee agencies, then it is my view, and I believe it was the general [p.85] thinking of the people I worked with, that once that transfer of funds had occurred, they no longer became federal funds. I view it as an event cycle.

Today a guarantee agency submits a bill for a program purpose which is lawfully a component of the program. It can't submit a bill for shoe laces. The Federal Government operationally examines the bill, enters data, cuts a check and makes the check payable to the guarantee agency and it goes out there, and then the statutory schema of the Higher Education Act provides for a period of time within which the agency must maintain records that are open to audit and review by the Department. And if some period subsequent to those funds being transferred or remitted to the agency an audit or review reveals that a portion of them was overpaid or was miss spent or was not adequately documented under the Department's regulations, then the Department has the

extended right to require that some or all of those funds be pulled back.

Once the whatever period of time the maximum period of time is for the retention of [p.86] those records and so on closes, it's akin in my mind to a statute of limitations, then there is no ability to recall those funds. So it's sort of like a tentative close and then a final close on those funds, and that's how I view it.

Q. And that's how it was viewed by the Department during your tenure from 1981 to 1988?

A. As far as I know. I never heard during my tenure in the Department any views different from that view.

Q. And that would explain why after the federal advances had been repaid by any individual guarantee agency, the remaining goal of the Federal Government would have been to regulate the operations of that agency?

MR. SUBAR: Object as to form.

A. I believe so, yes.

* * *

[p.110]

Q. Was there ever an assertion during your tenure from 1981 to 1988 with the Department of Education that any assets of a guarantee agency other than advances were federal in nature?

MR. SUBAR: Object as to form.

A. I think I responded to that earlier, and generally, no.

* * * * *